

Message Text

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PAGE 01 JAKART 01850 100108Z

ACTION EA-09

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FM AMEMBASSY JAKARTA

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TAGS: EFIN, ID

SUBJECT: BANK BUMI DAYA PROBLEM

REF: STATE 24573

1. SUMMARY: IRRUGULARITIES IN LOAN PORTFOLIO FORCE RESIGNATION OF CHAIRMAN OF BANK BUMI DAYA (BBD). ALTHOUGH UNSOUND LOANS MAY TOTAL ABOUT \$200 MILLION, AS STATE-OWNED BANK BBD EXPECTED TO WEATHER PROBLEM. BANK'S SITUATION IS OF LITTLE DIRECT CONSEQUENCE TO U.S. BUT BBD SCANDAL TENDS TO UNDERMINE BUSINESS CLIMATE. HOPEFULLY REFORMS MAY BE UNDERTAKEN. END SUMMARY.

2. CHAIRMAN AND BOARD OF DIRECTORS OF STATE-OWNED BANK BUMI DAYA (BBD) RESIGNED EN MASSE NEAR END OF JANUARY. MINISTER OF FINANCE ACCEPTED CHAIRMAN'S RESIGNATION AND TRANSFERRED ONE OTHER BBD DIRECTOR TO ANOTHER STATE BANK. MANAGEMENT OF BANK NOW BEING CLOSELY MONITORED BY BANK OF INDONESIA OFFICIALS.

3. RESIGNATIONS CAME AFTER MONTHS OF RUMORS TRIGGERED BY AUDIT OF BBD LOAN PORTFOLIO AND ACTUAL RESIGNATIONS GAVE RISE TO NEW FLURRY OF SPECULATION OVER MAGNITUDE OF QUESTIONABLE LOANS AUDITORS FOUND ON BBD'S BOOKS.

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ALTHOUGH FINANCE MINISTER ATTEMPTED GLOSS OVER SITUATION, DESCRIBING DIRECTORSHIP CHANGES AS "INTERNAL CONSOLIDATION" PROMPTED BY RAPID GROWTH IN BBD, BANKING SOURCES INFORM US THAT BBD'S BAD LOANS ARE ENORMOUS WITH ESTIMATES RANGING FROM \$100 MILLION TO \$500 MILLION. LATTER FIGURE STRIKES US AS HIGH BUT, BEARING IN MIND AN EVALUATION OF THE SOUNDNESS OF LOANS

IS A MATTER OF JUDGEMENT, WE WOULD GUESS THAT IF PROPER BANKING PRACTICES WERE INTRODUCED BBD WOULD PROBABLY HAVE TO WRITE OFF LOANS OF AROUND \$200 MILLION.

4. BBD IS STATE-OWNED BANK AND THERE IS LITTLE POSSIBILITY OF IT GOING OUT OF BUSINESS BECAUSE OF SIZE OF OVERDUE AND UNCOLLECTABLE LOANS ON ITS BOOKS. CONSEQUENTLY, IN OUR VIEW, CHAIRMAN'S RESIGNATION AND REASONS THEREFOR HAVE RELATIVELY LITTLE DIRECT FINANCIAL SIGNIFICANCE FOR U.S. OR OTHER FOREIGN CREDITORS. INDIRECT FINANCIAL IMPLICATIONS ARE PERHAPS MORE IMPORTANT PARTICULARLY IN LIGHT OF FACT THAT MANY SOURCES HERE TELL US PROBLEM IS BY NO MEANS CONFINED TO BBD. OTHER STATE-OWNED BANKS (THERE ARE FIVE OF WHICH BBD IS LARGEST) REPORTEDLY ALSO HAV LARGE AMOUNTS OF OVERDUE OR UNCOLLECTABLE LOANS ON THEIR BOOKS.

5. EXPANSION OF BANK CREDITS HAVE BEEN AMONG THE FACOTRS ADDING TO INFLATIONARY PRESSURES. SINCE STATE BANK CANNOT EASILY GO BROKE, EXTENT TO WHICH CENTRAL BANK MUST BAIL THESE BANKS OUT HAS SAME INFLATIONARY IMPACT AS PRINTING MONEY. ESPCIALY IMPORTANT IS GENERALIZED LOSS OF CINFIDENCE IN BOTH BANKING SYSTEM AND BUSINESS CLIMATE WHICH UNEARTHING OF SCANDALS SUCH AS BBD PROBLEM ENTAILS. REPORTEDLY, A SIGNIFICANT PORTION OF BBD'S DEFAULTED LOANS WERE MADE TO QUESTIONABLE ENTERPRISES WHICH WERE BACKED EITHER BY HIGH GOVERNMENT OFFICIALS OR BY BUSINESSMEN FRONTING FOR SUCH OFFICIALS. WE ARE TOLD THIS PRACTICE OF TAPPING STAT BANKS FOR SUCH LIMITED OFFICIAL USE

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CREDITS IS FAIRLY WIDESPREAD.

6. THERE HAS BEEN AT LEAST ONE FAVORABLE RESULT FROM BBD SCANDAL. CHAIRMAN OF SUPREME CREDIT BOARD (BEPEKA, A CONSTITUTIONALLY-ESTABLISHED OVERSIGHT ORGANIZATION) APPARENTLY EMBARRASSED BY SCANDAL AND INEFFECTIVENESS OF HIS ORGANIZATION HAS COMPLAINED TO PRESS AND TO PARLIAMENT THAT BEPEKA IS A "TOOTHLESS WATCHDOG." HE IS QUOTED AS SAYING THAT ONLY 30 PERCENT OF GOVERNMENT ENTERPRISES (INCLUDING STATE BANKS) EVEN BOTHER TO SUBMIT FINANCIAL REPORTS AND BALANCE SHEETS AND BEPEKA CANNOT, APPARENTLY, COMPEL THEM TO DO SO. IN BANK SECTOR, HE SAID, BANKERS CAN SIMPLY REFUSE TO DIVULGE INFORMATION REQUESTED BY BEPEKA ON GROUNDS IT IS A "BANK SECRET." WHETHER REFORMS BEPEKA HAS CALLED FOR WILL BE UNDERTAKEN REMAINS TO BE SEEN.

NEWSOM

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